

**INVESTMENT CLIMATE STATEMENT
JAPAN**

JULY 2002

U.S. EMBASSY TOKYO

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A.1. Openness To Foreign Investment: Few Formal Restrictions

Japan, the world's second-largest economy, is an immense potential market for U.S. foreign direct investment (FDI). The Government of Japan (GOJ) imposes few formal restrictions on FDI in Japan, and has removed or liberalized most legal restrictions that apply to specific economic sectors. The government does not impose export-balancing requirements or other trade-related FDI measures on firms seeking to invest in Japan. Moreover, risks associated with investment in many other countries, such as expropriation and nationalization, are not an issue in Japan.

The current low-growth environment in Japan has created many new opportunities for FDI in this extremely rich and broad market:

- Prices are down to their lowest point in a decade.
- More Japanese companies are actively looking for foreign partners to inject needed capital and know-how.
- There are distressed assets that can be profitably acquired and returned to economic viability.

The challenges facing foreign investors seeking to establish or enhance their presence in Japan -- many of the most important of which are matters of private business practice rather than of government regulation -- include:

- A high overall cost structure that makes market entry, exit, and expansion expensive;
- Cultural and linguistic challenges to doing business;
- Corporate practices and market rules that inhibit foreign acquisition of Japanese firms, such as insufficient financial disclosure practices, cross-holding of shares among companies belonging to the same business grouping (keiretsu), the low proportion of publicly traded common stock relative to total capital in many companies, and public attitudes about foreign takeovers;
- Exclusive buyer-supplier networks and alliances are still maintained by some "keiretsu," which limit competition from foreign firms and domestic newcomers;
- Laws and regulations that directly or indirectly restrict the establishment of business facilities and hinder market access for foreign products, services, and FDI.
- Labor practices which inhibit labor mobility, repress productivity, and negatively impact development of skills.

All of these issues are currently being addressed in government-to-government talks, and progress is being made in many areas.

Despite Japan's attractive characteristics as a potential investment site, however, FDI levels have remained small relative to the size of the economy. In JFY 2001, Japan's annual inward FDI totaled \$ 17.3 billion, or 0.4% of GDP. Although investment in Japan is up over 300% since FY97, the JFY 2001 statistics showed a considerable decline over the previous year's performance. Japan continues to host the smallest amount of inward foreign investment as a proportion of total output of any major OECD nation. Foreign participation in mergers and acquisitions (M&A), which account for some 80% of FDI in other OECD countries, although on an upward trend, also lags in Japan. Meanwhile, Japan continues to run an imbalance between

its inward and overseas FDI (see Table 1). In JFY 2001, Japan reportedly invested \$ 31.1 billion overseas, (down from \$ 49.2 the previous year). Japan's relative lack of foreign investment also acts as a restraint on the expansion of imports.

Much of the FDI flows in recent years, have come in the financial services and telecommunications sectors, reflecting important restructuring in these areas.

In the past four years, ongoing economic restructuring (due in large part to the more competitive financial sector and greater emphasis on rate of return), and changes in Japan's financial markets contributed to growth in foreign direct investment in Japan in non-financial sectors. Distribution affiliations, joint ventures, and mergers and acquisitions involving foreign and Japanese financial services providers have accelerated rapidly, as foreign firms take advantage of business opportunities being created in Japan's financial sector as a result of the Japanese government's "Big Bang" and the U.S. government's deregulation initiative with Japan. Japanese financial firms have started to look overseas for assistance in the form of new products, technologies and capital to meet these challenges. In addition, foreign firms have stepped in to buy the assets of domestic financial services firms that have recently failed. At the same time, structural impediments to foreign investment remain, and it is not certain that inward foreign investment flows will continue to accelerate.

Acknowledging that FDI in Japan lags far behind that of other industrialized economies, the GOJ has in recent years taken some welcome steps to address investment-related problems. Of most recent significance is the GOJ initiative to revise the Commercial Code. Other legislation reforming bankruptcy procedures has provided M&A opportunities, as distressed Japanese companies are able to seek partners or buyouts. Generally speaking, there are strong indications that the Ministry of Economy, Trade and Industry (METI) in particular is taking seriously the challenge of attracting greater foreign investment to Japan. At the regional level, a number of prefectural and city governments are intensifying their efforts to attract foreign investors.

Liberalization of Investment Restrictions: Japan has gradually eliminated most of the formal restrictions governing its FDI regime. In 1991, the GOJ amended the Foreign Exchange and Foreign Trade Control Law (which also controls foreign investment) to replace the long-standing "prior notification" requirement for all FDI with an "ex post facto notification" requirement for investment in non-restricted industries. "Prior notification" (and thus case-by-case approval) is now required only for investment in certain restricted sectors, including agriculture, forestry, petroleum, electrical/gas/water utilities, aerospace, telecommunications, and leather manufacturing. Administrative approval for foreign investment in some of these sectors is quite certain, while in other sectors it is likely to be subject to greater scrutiny based on "national sovereignty" or national security concerns.

U.S. investment has become increasingly common in some traditionally restricted sectors, particularly in the petroleum and telecommunications industries. In February 1998, all restrictions on foreign ownership were removed with respect to Type I telecommunications carriers including their radio stations (with the exception of NTT and KDD). In the fall of 2001, a European telecommunications group took control of one of Japan's competing telecom operators with an \$11 billion investment, currently the single largest foreign investment in Japan. Restrictions on foreign ownership in KDD were abolished in July 1998, and a June 2001

amendment to the NTT Law raised the ceiling on foreign investment in NTT from twenty percent to one third. Foreign investment restrictions on cable television and communications satellite broadcast operators have also been lifted.

Several sections of the Japanese Antimonopoly Law (AML) are relevant to FDI. For example, chapter four of the AML includes extensive antitrust provisions pertaining to international contract notification (section 6), stockholding (section 10, 14), interlocking corporate directorates (section 13), mergers (section 15), and acquisitions (section 16). The stated purpose of these sections is to restrict any stockholding, management, joint venture, and M&A activities that constitute unreasonable restraints on competition or involve unfair trade practices. These provisions are not intended to discriminate against foreign companies or to discourage FDI.

Limitations on Facility Development, and Availability of Investment Real Estate:

While the price of real estate has fallen for 11 consecutive years (since 1992), potential foreign investors still find that high real estate-related expenses and regulations are obstacles to investment in Japan. Urban land prices, (although less than half the 1991 high) remain expensive, and the rate of property turn-over is slow enough that investors frequently have trouble assembling property of sufficient size to accommodate their operations. Lack of information on land prices and ownership also impedes foreign and domestic investors, by making it harder to assess the real asset value of potential business partners or acquisition targets. It also inhibits faster development of the domestic market for estate-related financial products.

Revisions to the Securities Investment Trust Law, enacted in November, 2000, lifted the ban on real estate investment trusts (REITs) to permit marketing of mutual funds that invest in property rights. Although growth has been slow, REITs are already increasing demand for transparency and accurate pricing in the real estate market.

Aiming to increase the liquidity of Japanese real estate markets, over the recent years the government has progressively lowered capital gains, registration, and license taxes on real estate. Changes in tax policy and accounting standards could increase real estate liquidity, but the market is still hampered by the shortage of legal and accounting professionals, the lack of information on prices and income flows, and taxes that discourage real estate transactions. Beginning March 31, 2001, the Japan Institute of Certified Public Accountants introduced a standard requiring companies to write off substantial losses (50% or more) on real estate inventories acquired for sale or development, further encouraging liquidity in real estate markets.

Japan continues to restrict the development of industrial and commercial facilities in some areas in an attempt to prevent excessive concentration of development in the environs of Tokyo, Osaka, and Nagoya, and also to protect land designated as optimal for agriculture. On the other hand, many prefectural governments outside the largest urban areas will make available property in public industrial parks. Generally speaking, Japan's zoning laws give local Japanese officials and residents considerable discretionary authority to screen almost all aspects of a proposed building. These factors effectively reduce the real estate available for development and often lead to delays in construction and higher building costs.

The Large-scale Retail Store Location Law (LRSLL) took effect on June 1, 2000. The

law emphasizes the preservation of the living environment rather than the protection of small business. Local authorities implement the law in accordance with guidelines laid down by the Ministry of Economy, Trade and Industry (METI). The new law needs to be closely monitored to ensure that foreign and domestic large retailers do not experience difficulty establishing retail facilities under the locally administered rules.

Corporate Tax Treatment: Local branches of foreign firms are generally taxed only on corporate income derived from within Japan, whereas domestic Japanese corporations are taxed on their worldwide income. Calculation of taxable income and allowable deductions, and payments of the consumption tax (sales tax), are otherwise the same as those for domestic companies, with national treatment for foreign firms. Corporate tax rules classify corporations as either foreign or domestic depending on the location of the head office, without regard to the place of incorporation. The U.S.-Japan Tax Treaty provides for the avoidance of double taxation.

Dividends distributed by a domestic Japanese firm are subject to a 20 percent withholding tax; interest payable to a nonresident is normally subject to withholding of 15 percent, and royalties and fees paid to a foreign licensor by a Japanese licensee are subject to normal withholding of 20 percent. The U.S.-Japan Tax Treaty reduces tax on dividends, withholding and royalties to 10 percent. A special tax measure allows designated inward investors to carry over certain losses for tax purposes for ten years rather than for the normal five years. In JFY96, the scope of losses that qualify for this special measure was expanded.

As part of the JFY99 Tax Reform, Japan's effective corporate tax rate, including local taxes, was reduced from 46.36% to 40.87%.

Legislation to introduce consolidated taxation, retroactive to April 1, 2002, is expected to pass the current Diet session by late June 2002. Consolidated taxation should facilitate investment and corporate restructuring, because the losses usually expected from a new venture or recently-acquired subsidiary can now be charged against the profits of the parent firm or holding company. However, in order to partially recapture the anticipated loss in tax revenues, for the next two years the GOJ plans to institute a 2% tax surcharge on firms that elect consolidated taxation.

Investment Incentives: The government-owned Development Bank of Japan (DBJ) offers foreign-affiliated firms various lending programs under which foreign-owned companies (companies whose foreign capital ratio is one-third or higher) are eligible for low interest, long-term loans for capital investment. The loan amount may be up to 60% of the total investment amount and the loan period can run as long as 30 years. Interest rates are roughly competitive with the private long-term prime rate. Similar low-interest loan programs for foreign firms have been established by the Okinawa Finance Corporations as incentives to foreign firms investing in this region. In addition, DBJ will continue to offer special incentives to investors interested in the Hokkaido-Tohoku area.

The "Technopolis" project, sponsored by METI, is available to both Japanese and foreign firms. Under this program, METI and prefectural governments can provide various types of assistance (e.g., preferential depreciation and land taxes) to companies locating in areas designated for development as a technology-intensive zone. As of 1999, there were 26 areas throughout Japan with the Technopolis designation.

The GOJ has made efforts to improve the dissemination of FDI-related information and to facilitate investment opportunities through various government support services. The DBJ supports foreign companies by supplying market information on Japan (general data on industries, market scale, distribution channels, etc.) and by serving as consultants on specific investment projects. In June 1993, the GOJ established a business information support firm, called the Foreign Investment in Japan Development Corporation (FIND), which (for a fee) advises foreign firms on the many challenges and opportunities of investing in Japan and facilitates meetings with potential investment partners. FIND also publishes annual statistics on FDI in Japan and maintains detailed reference aids on FDI, such as local-level FDI programs.

The Japan External Trade Organization (JETRO) established an "Invest-in-Japan" Division. Its activities to promote inward investment include investment promotion seminars both in Japan and the US and Europe to foreign investors, extensive English-language materials on issues affecting foreign investment, such as tax laws, regional incentives etc.

Japanese local governments have in recent years shown increasingly sharp interest in attracting foreign investors to their districts. Most prefectural governments now offer an array of investment incentives including direct subsidies, and assistance in the form of grants and loans for facilities construction, and aid in paying for worker training and even worker salaries. In international comparison, however, these incentives still appear small in scale. Typically, even if a potential investing firm meets all of a prefecture's various criteria, the maximum incentive it can hope to receive has a value of less than \$10 million.

However, local government investment promotion efforts are hampered by the lack of tax breaks and the fact that the local government may set rigid conditions to qualify for incentives. Local government investment incentives also tend to be one-time, not lasting, and with the exception of the national government-sponsored incentives for investment in depressed areas, not related to taxes. This is because Japanese prefectures, not in control of their own tax laws, are not in a position to change them or interpret them flexibly.

In general, although the Japanese government's FDI promotion efforts are well intentioned, many U.S. firms have often found that incentive programs are insufficient in scope to overcome other problems they face.

A.2. Conversion and Transfer Policies: Generally Uninhibited

All foreign exchange transactions to and from Japan -- including transfers of profits and dividends, interest, royalties and fees, repatriation of capital, and repayment of principal -- are, in principle, freely permitted unless expressly prohibited. With the April 1998 revision of the Foreign Exchange Law, Japan moved to an ex-post notification system. This means that all foreign exchange transactions (unless specifically prohibited, including certain foreign direct investments, listed in the Appendix) no longer require prior notification or approval. In addition, the new law eliminated the authorized foreign exchange bank system, whereby foreign exchange transactions all had to go through certain registered banks. All other restrictions on methods of payment -- including netting of settlements -- were also removed, enhancing the ability of foreign and Japanese financial firms to offer a fuller range of services in Japan. This has led to lower foreign exchange transaction costs for non-financial firms as well.

Japan is an active partner in the struggle to choke off terrorist financing. In coordination with other OECD members, the GOJ is strengthening due-diligence requirements for financial institutions and tightening know-your-customer procedures. These changes could have an impact on the transfer of funds.

A.3. Expropriation and Compensation: Virtually No Risk

In the post-war period, the GOJ has not expropriated or nationalized any enterprises, with the exception of the nationalization in 1998 of two large capital-deficient banks and, in 2002, of two small failed regional banks. Expropriation or nationalization of foreign investments is unlikely in the foreseeable future.

A.4. Dispute Settlement: No Outstanding Cases in Investment Area

There have been no major bilateral investment disputes since 1990, and there are no outstanding expropriation or nationalization cases in Japan. There have been no cases of international binding arbitration of investment disputes between foreign investors and the GOJ since 1952. Japan is a member of the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitration Awards. However, it has long been considered an inhospitable forum for international commercial arbitration. The Japan Commercial Arbitration Association, the only organization that arbitrates international trade-and investment-related disputes, had only 58 cases submitted to it between 1996 and 2000. Of these, only 34 went to arbitration.

There are no legal restrictions on access by foreign investors to Japanese lawyers. However, strict limitations on legal practice in Japan by foreign lawyers, a prohibition on Japanese lawyers joining foreign-based law firms, and the small number of Japanese lawyers capable of handling international business transactions all constrain the ability of foreign investors to obtain adequate legal advice on doing business in Japan.

Foreign lawyers licensed in Japan under the 1986 Foreign Lawyers Law are still not allowed to advise foreign investors on many aspects of investing in Japan, since such advice is considered as the practice of Japanese law. The unnecessarily restrictive provisions of Japanese law and the rigid enforcement of these restrictions by the Federation of Japanese Bar Associations (*Nichibenren*) deprive foreign investors of the opportunity to receive the optimal combination of legal advice that a system more in conformity with modern standards of international legal practice would allow.

However, the Judicial Reform Council, an advisory body to the Prime Minister, recommended in June 2001 a large number of changes to Japan's legal system, many of which address current shortcomings. Among the Council's recommendations were deregulating the requirements for specified joint enterprises and to study the restriction that prohibits foreign lawyers from hiring Japanese lawyers (even though Japanese lawyers are allowed to hire foreign lawyers). More generally, there is still no definite policy to move toward completely free association between foreign and domestic lawyers, a change that would do the most to eliminate current bottlenecks.

Still, there has been significant movement. The Judicial Reform Promotion Headquarters was established on December 1, 2001, based on the Law on Promotion of Judicial Reform. The Headquarters has developed a reform program, based on the recommendations of the Judicial Reform Council. On March 19, 2002, the Cabinet adopted a program which provides for the following:

- To increase the number of legal professionals, the Ministry of Justice (MOJ) will increase the annual number of persons who pass the Bar Examination to 1,200 by the end of 2002, to 1,500 by 2004 and to 3,000 by around 2010; and the Headquarters, in cooperation with the Ministry of Education, Culture, Sports, Science and Technology, will introduce a new system of law schools, commencing in April 2004, and in preparation will develop standards for selecting the universities that will be allowed to establish law schools.
- To reform the arbitration law, the Headquarters will submit legislation to the Diet in mid-January 2003, which will include a major revision of the existing Arbitration Law and improvement of the legal framework for arbitration, including international commercial arbitration.
- To increase the speed and efficiency of civil litigation, the Headquarters and MOJ will submit legislation to the Diet in mid-January 2003 to reduce by half the length of time required to complete court trials through measures to promote efficient scheduling of hearings, increase significantly the number of judges and court personnel, and facilitate litigants' collection of evidence at early stages of litigation.
- The Headquarters and MOJ will submit legislation to the Diet in mid-January 2003 to reduce filing fees for civil litigation.
- To strengthen judicial oversight over administrative agencies, the Headquarters is undertaking a comprehensive study of judicial oversight over administrative agencies, including review of the Administrative Case Litigation Law, and will take necessary measures to strengthen judicial oversight by November 30, 2004.
- To make the specialized departments concerning intellectual property rights in both the Tokyo and Osaka District Courts function substantially as "patent courts," the Headquarters and MOJ will submit legislation to the Diet in mid-January 2003.

Japan's civil courts enforce property and contractual rights, and the courts do not discriminate against foreign investors. However, they are sometimes ill suited for litigation of investment and business disputes. As in many other countries, Japanese courts operate rather slowly. As noted above, the Judicial Reform Promotion Headquarters is enacting a number of changes to speed the conduct of trials.

In addition, the courts lack contempt powers to compel a witness to testify or a party to comply with an injunction, and timely temporary restraining orders and preliminary injunctions are very difficult to obtain. While filing fees for large civil cases were reduced in 1992, they are still based on the amount of the claim, rather than a flat fee. Lawyers usually require large up-front payments from their clients before filing a lawsuit, with a modest contingency fee, if any, at the conclusion of litigation. Contingency fees familiar in the U.S. are relatively uncommon. A

losing party can delay execution of a judgment merely by appealing, and in appeals to the high courts, additional witnesses and other evidence are sometimes allowed.

Courts do have power to encourage mediated settlements, and the courts have a supervised mediation system. Parties can manipulate this system to delay resolution, however, and because judges move frequently, continuity is often lost. As a result, it is very common for companies to settle out of court.

The very small number of lawyers in Japan is also a significant impediment to dispute resolution. As noted above, this will be considerably increased over the next ten years. But because there are so few lawyers in Japan now, these increases by themselves will not be sufficient to remedy the shortage of legal services available in Japan in the near future, even if they are implemented quickly.

A new Product Liability Law became effective in July 1995, but to date there have been only a few court cases. However, many companies have modified their design and production processes, as well as provided more detailed instruction and product manuals, in an effort to limit potential liability. Twelve industry associations established a Product Liability Center in order to take care of complaints based on the Product Liability Law. Those industries are: pharmaceuticals, chemical products, gas/kerosene equipment, household electrical appliances, automobiles, housing materials, daily necessities (two centers), beverages, cosmetics, fire-prevention products, and leisure boats. In the five years from JFY 1995 to JFY 1999, these Centers addressed a total of 54,351 complaints.

A.5. Performance Requirements and Incentives: None

Japan does not maintain a system of performance requirements. Japan also maintains no formal requirements for local management participation or local control in joint ventures or other forms of direct investment, except in restricted sectors.

A.6. Right to Private Ownership and Establishment: Secure for Foreign Business

Japan secures the right for foreign and domestic private enterprises to establish and own business enterprises and engage in all forms of remunerative activity.

A.7. Protection of Intellectual Property Rights: Can Be Time-Consuming And Costly

Protection of intellectual property rights is an integral part of every successful U.S. exporter's basic market strategy in Japan. It is necessary to file applications to register patents and trademarks in Japan to obtain protection, but prior patent filing in the United States can provide certain advantages if applications are filed promptly in Japan. A U.S. patent or trademark attorney can provide informal advice, but it is necessary to hire a Japanese lawyer or patent practitioner (benrishi) registered in Japan to prosecute the patent or trademark application. In conformity with international agreement, Japan maintains a non-formality principle for copyright registration -- i.e., registration is not a pre-condition to the establishment of copyright protection. However, the Agency of Cultural Affairs maintains a registry for such matters as date of first publication, date of creation of program works, and assignment of copyright. U.S. copyrights are recognized in Japan by international treaty. U.S.-produced semiconductor chip

design-layouts are protected for ten years under a special law if they are registered with the Japanese “Industrial Property Cooperation Center”-- a Japanese government-backed public corporation.

Obtaining and protecting patent and trademark rights in Japan can be time-consuming and costly, although patent fees have recently been reduced considerably. While the process to safeguard such rights might seem prohibitive, lack of protection would permit competitors both in and outside of Japan to copy a product or production process. Even when intellectual property rights have been acquired, pirating of technology and designs can occur in Japan, as in other countries. Each company in a trading or licensing agreement should understand clearly what its rights and obligations are with respect to the intellectual property rights owned or acquired by the other. Such a clear understanding helps to create a good rapport based on mutual trust, thereby ensuring the success of the trading or licensing agreement.

Patents, Trademarks, Utility Models and Designs: Unlike U.S. patent law, patents are granted to the first to file an application for a particular invention, rather than to the first to invent. Although Japan accepts filings in English (to be followed by a Japanese translation), companies should ensure that translations of their applications are perfect, as significant negative ramifications may result from translation errors. Prompt filing in Japan is crucial because printed publication of a description of the invention anywhere in the world, or knowledge or use of the invention in Japan, prior to the filing date of the Japanese application, would preclude the grant of a patent on the application. Also, unlike the United States, where examination of patent applications is automatic, an applicant must request examination of his patent application in Japan within three years of filing. (Reduced from seven years to three years starting October 1, 2000.)

As is true in many countries, all patent applications are published 18 months after filing. If, during the examination, the Japanese Patent Office (JPO) finds no impediment to the grant of a patent for a particular invention, it publishes the patent application in the Patent Public Gazette a second time, including any changes that have been made during the examination. Under a recent amendment to the Patent Law, parties may contest the terms of a patent grant immediately after issuance by the Patent Office (for a period of up to six months), rather than prior to registration as had been the previous practice. The patent is granted and valid for 20 years from the date the application is filed.

It takes an average of 21 months, according to the latest JPO statistics in CY 2000, in Japan from the request for examination of application to First Action -- compared to 18 months in the United States for the entire patent process. An applicant can request accelerated examination, and efforts by the Patent Office to make the documentation necessary for the preliminary research required to request accelerated examination available electronically are expected to lower the cost of such requests to the applicant. During the examination period, limited effective legal protection exists.

Japan's Trademark Law protects trademarks and service marks. As is the case with patent applications, a resident agent (usually a lawyer or patent agent) must prosecute the trademark application. And as with the processing of patent applications, Japan's trademark registration process can be slow. Any company planning on doing business in Japan should file for trademark registration as early as practicable. Japan is subject to the Madrid Protocol

(effective March 14, 2000) and trademarks registered at the WIPO Secretariat will be protected among member countries.

Japan's Utility Model Law also allows registration of utility models, a form of minor patent with a 6-year term of protection, retroactive from the date of application since January 1994. A separate design law allows protection of designs, with a 15-year term of protection from the date registration was made.

Unfair Competition and Trade Secrets: The only protection available for a trademark in Japan prior to registration is under the Japanese Unfair Competition Prevention Law. Under this law, the owner of the mark must demonstrate that the mark is well known in Japan and that consumers will be confused by the use of an identical or similar mark by the unauthorized user. In 1990, Japan enacted amendments to the law that provided some protection from theft of trade secrets, such as know-how, customer lists, sales manuals, and experimental data. The law, which was amended completely in 1993, also provides for injunctions against wrongful use, acquisition, or disclosure of a trade secret by any person who knew or should have known that the information in question was misappropriated. The judicial process, however, makes the enforcement of rights without loss of trade secrets difficult.

A.8. Transparency of the Regulatory System: Toward More Openness

Over-regulation in Japan continues to restrain economic growth, raise the cost of doing business, prevent competition from nurturing market-based efficiencies in the private sector, and impede investment. It also raises prices and increases the cost of living for Japanese consumers. The 1990s have been dubbed Japan's "Lost Decade", during which Japan's growth in gross domestic product (GDP) averaged a mere 1.6%, or less than half the 3.8% average of the preceding decade. This was brought about by Japan's inability to recover from massive asset deflation in the wake of the burst economic "bubble" of the early nineties (manifested in huge non-performing loans) and an inability to reform political, economic and social systems to adapt to the changing international environment of economic globalization and the Information Technology revolution. Typical of highly regulated economies, the Japanese economy is now suffering from a serious misallocation of resources, a lack of investment and a lack of entrepreneurial innovation. In addition to slowing growth, government over-regulation lies at the heart of many market access problems faced by U.S. companies doing business in Japan.

An essential prerequisite for a vibrant Japanese economy is a regulatory system that is transparent, fair, predictable and accountable. It is important that domestic and foreign firms alike have full access to information and opportunities to participate in the regulatory process. The Japanese Government has made the need for greater transparency a crosscutting theme of its Three-Year Program for Promoting Regulatory Reform (Cabinet Decision of March 30, 2001). The systemic measures set out in the Three-Year Program could contribute to needed improvements in the transparency and accountability of the Japanese regulatory system. They include: the strict enforcement and promotion of the use of the 1994 Administrative Procedure Law; increased transparency of administrative guidance; full and effective implementation of the Law Concerning the Disclosure of Information Retained by Administrative Agencies; wide and effective use of the Public Comment Procedures for Formulating, Amending and Repealing Regulations; introduction of the "No Action Letter" system; comprehensive and objective

evaluation of the regulatory process; and examination of the need, effects, and costs of new proposed regulations.

Building on these measures, the United States in its Regulatory Reform Initiative submission has recommended that the Japanese Government undertake additional improvements in its regulatory system to support Japan's reform efforts and ensure universal access to government information and the policymaking process. In particular Japan needs to make the Public Comment Procedures more effective, to reduce the use of Administrative Guidance, and to allow for greater public participation in the legislative process.

Under the Antimonopoly Law, the Japan Fair Trade Commission (JFTC) is authorized to screen certain notifiable international contracts--such as joint ventures involving foreigners--and to prohibit specific contracts that, in the JFTC's judgment, might cause unreasonable restraints on trade or involve the use of unfair trade practices. In June 1997, however, the JFTC abolished its contract notification system, under which any Japanese entrepreneur who enters into an international contract that was notifiable under JFTC rules was required to file with the commission within 30 days of concluding such an agreement. The JFTC has also abolished 33 antitrust-exempted cartels, with four other exempted cartels scheduled to be eliminated in future years, leaving three antitrust-exempted cartels operating in Japan. In October, 1999 the U.S. and Japan concluded a bilateral Antitrust Cooperation Agreement under which several investigations and criminal prosecutions have been pursued.

The United States continues to hold bilateral working-level discussions in an effort to encourage the Japanese to promote deregulation, competition policy, and administrative reform measures that would increase imports and foreign direct investment into Japan. The reader should consult the National Trade Estimate Report on Foreign Trade Barriers, issued by the Office of the U.S. Trade Representative (USTR) on March 31, 2002, for a detailed description of Japan's regulatory regime as it affects foreign firms (both exporters and investors).

A.9. Capital Markets and Portfolio Investment: Some Restrictions

Japan maintains no formal restrictions on inward portfolio investment, and in fact foreign capital occupies an increasingly important place in Japanese capital markets. However, corporate practices such as cross-shareholding, while declining, still limit the percentage of shares in individual firms and in the overall market that foreign investors can actually purchase. Informal restrictions on management participation of foreign shareholders limit the attractiveness of Japan's equity market to foreign investors, although some firms are taking steps to facilitate exercise of shareholder rights by foreign investors, such as permitting electronic proxy voting, beginning April 1, 2002.

Environment for Mergers and Acquisitions: Stock market-based takeovers of listed firms via tender offer, as widely practiced in the United States and parts of Europe -- both friendly and hostile -- remain rare in Japan. Japan's famous aversion to M&A activity is starting to fade, accelerated by the unwinding of extensive corporate cross-shareholding brought about by implementation of improved accounting standards. Tender offers for listed firms may increase as newly-listed firms in the over-the-counter (OTC) market -- which are less likely to become predominantly "cross-held" -- increase. But viewed historically, of the roughly 400 foreign investment M&A transactions in Japan since 1991 (including divestitures of overseas

firms held by Japanese), only five cases involved tender offers for companies listed in Japan. (Even this was an improvement over the previous two decades, which saw only one such case.) The "acceleration" of tender offer activity in the 1990's stems directly from the 1990 elimination of the prior-to-offer reporting requirement (which stipulated that the Finance Ministry be informed of any tender offer nine days before its announcement) and the extension of the tender offering period to 60 days.

Friendly transfer of wholly-owned and majority-owned subsidiaries is a more common form of M&A in Japan. Similarly, there are signs that owner-operated unlisted firms -- which traditionally would only sell out as a last resort before bankruptcy -- are becoming more amenable to acquisition by foreigners. Particularly in the more modern, more service-oriented sectors of the economy, purchase by foreigners is becoming less of a badge of shame than in years past.

Still, there remain a number of key factors limiting greater entry into the Japanese market through M&A with unlisted firms -- including tax policy, weak accounting and disclosure practices, Japan's underdeveloped OTC stock market (which if more developed would reduce the risks involved in M&A), lack of readily available information on firms that might be acquired, and the relative lack of a M&A "infrastructure" in the form of specialists skilled in making matches and structuring M&A deals.

The past several years saw introduction of two new exchanges geared towards encouraging start-ups and venture capital investments. In December 1999, the Tokyo Stock Exchange introduced "Mothers," with less-stringent listing criteria for emerging companies. In April, 2000, TSE announced it would tighten listing requirements and screening procedures (requiring new companies to post a full year of earnings before being listed) to prevent firms with organized crime from listing on the exchange. There are now 36 firms listed on Mothers.

NASDAQ Japan now has 88 listed companies, up from the eight with which it opened June 19, 2000. Although Mothers and NASDAQ still have relatively few listed firms and suffer from lack of liquidity, analysts expect the exchanges to develop a healthy competition and provide needed capital for entrepreneurs.

Commercial Code Revisions: In January 2001, new laws designed to facilitate procedures for spin-offs to establish new firms and to transfer divisions from one company to another went into effect. A major revision of the Commercial Code is now underway. The Ministry of Justice has indicated that it intends to introduce legislation to the Diet in 2002 that will significantly increase the flexibility of capital structure and improve corporate governance:

Flexibility of Capital Structure:

As detailed in the document "Japanese Corporate Law: Drastic Changes in 2000-2001" issued by the Ministry of Justice on April 16, 2002, the Diet has enacted or is expected soon to enact a number of revisions to the Commercial Code to improve the methods through which companies may obtain financing and services and to provide incentives to managers and employees, including amendments:

1. Relaxing the restrictions on the size of units of stocks, including abolishing the ¥50,000 per share minimum issue price and restrictions on the minimum net assets per share at the time of stock splits;
2. Authorizing the issuance of tracking stock;
3. Eliminating the prohibition on the issuance of non-voting common stock, and increasing the limit on the total number of non-voting shares that may be issued from one-third of the total issued shares to one-half of total issued shares;
4. Substantially liberalizing restrictions on issuance of stock options, including abolishing restrictions on the recipients of stock options, maximum number of stock options that may be granted and the permissible exercise period;
5. Permitting classes of shareholders of closely held corporations that have issued more than one class of shares to elect a specified number or percentage of board members;
6. Eliminating the prohibition against transfers of new subscription rights; and
7. Eliminating the requirement for court-supervised inspection procedure for valuation of in-kind capital contributions, allowing as an alternative certifications by professionals such as lawyers, accountants or tax accountants.

Improvements in Corporate Governance:

In addition, the Diet has enacted or is expected soon to enact a number of revisions to the Commercial Code to ensure efficient corporate governance, including amendments:

1. Providing publicly traded companies the option of adopting U.S.-style corporate governance system instead of complying with the statutory auditor (*kansayaku*) requirement. This option would require the appointment of executive officers and the establishment of a board committee system in which at least the audit, nomination and compensation committees would be composed of a majority or more of outside directors; and
2. Permitting companies to use the Internet or other electronic means to provide notices of shareholders' meetings and other similar communications to shareholders upon individual consent, and permitting shareholders to exercise their voting rights through the use of electronic devices. In addition, companies will be permitted to meet their mandatory disclosure requirements for balance sheets (and profit and loss statements) by making the full text available for 5 years in an electronic format.

Cross-shareholding and M&A: Potential foreign investors in Japan frequently point out that extensive cross-shareholding (*mochiai*) in Japan greatly complicates market-based merger and acquisition transactions, and reduces the potential impact of shareholder-based corporate governance. Corporate governance practices which result in senior management emphasizing internal loyalties over shareholder return can also lead to premature rejection of M&A offers. At the same time, Japanese companies are unwinding cross-shareholdings, which has accelerated in recent years under the pressure of difficult corporate finances and stricter accounting

requirements. Similarly, more corporations are hiring outside directors, and placing greater emphasis on shareholder value in their management practices.

To assist corporations in reducing the unfunded liabilities of corporate pension funds and to accelerate the unwinding of cross-shareholdings, the Japanese government implemented legislation in 2000 that allows corporations to transfer shareholdings to their related corporate pension funds. The pension funds will be able to properly execute shareholder rights on the transferred shares, and sell the shares if it is deemed in the best interests of the pension-holders. However, many firms preferred the alternative of indirect transfer of shares through a trust whereby the sponsor corporation retains voting rights and effectively influences when the shares can be sold.

In another useful innovation, the Diet approved amendments to the Commercial Code permitting creation of a stock swap system, through which one of the parties becomes a wholly-owned subsidiary company and the other a parent company, as well as a stock transfer system to establish a parent company. Special tax treatment will be implemented in conjunction with the creation of the stock exchange and the stock transfer system to allow deferment of taxes on capital gains on stocks at the time of exchange and transfer. To take advantage of these new rules, however, foreign investors must legally establish a Japanese subsidiary firm to act as the counterpart to the stock exchange/transfer. Legislation to address the need to enable foreign firms – and Japanese firms operating internationally – to obtain similar tax benefits when conducting M&A's based in other markets has not been introduced, and indications are that the Ministry of Justice Legislative Council does not intend to recommend such legislation as part of the Commercial Code revisions.

In 2001 the GOJ created the Banks' Shareholdings Purchase Corporation to facilitate sale of bank cross-held shares.

Accounting and Disclosure: Accounting and disclosure standards are an extremely important element in assessing and improving any nation's environment for mergers and acquisitions. Before any merger or acquisition can take place, it is critical that the merging or purchasing corporations have the best possible information on which to make business decisions. Implementation of "Big Bang" -associated reforms since 1998 has significantly improved Japan's accounting standards.

Reporting and disclosure by unlisted firms and financial institutions -- determined by the Ministry of Justice-administered Commercial Code, not the Financial Services Agency (FSA)-administered Securities and Exchange Law -- remains the biggest accounting obstacle to investing. However, FSA guidelines do regulate unlisted financial institutions, including unlisted life insurance companies.

Aside from the lack of publicly available information about the accounts of unlisted Japanese companies (a situation which also exists in the United States), the greatest problem from the perspective of promoting foreign M&A had been the use of book-value accounting rather than mark-to-market accounting. Consolidated accounting is also critical to accurately pricing subsidiaries for sale or purchase.

Starting in JFY99, the shift to consolidated accounting became mandatory, and "effective control standards and influence" standards were introduced in place of conventional holding standards, expanding the range of subsidiary and affiliated companies included for the settlement of account. Consolidated disclosure of contingent liabilities, such as guarantees, began in April 1998.

From JFY00, all marketable financial assets held for trading purposes must be recorded at market value, except for cross-shareholdings and other long-term securities holdings for which market-value accounting was implemented in JFY01.

Also starting in JFY00, companies were required to disclose unfunded pension liabilities by valuing pension assets and liabilities at fair value. Fixed asset impairment accounting will become mandatory beginning in FY05. The new rule will require firms to realize losses if the recoverable value of property, plant or equipment is significantly less than book value.

The greater focus on consolidated results and mark-to-market accounting is already having an impact and is encouraging unwinding of cross-held shares. Corporate restructuring is accelerating, and companies are rushing to reduce pension under-funding. Banks have started disposing of low-yield assets. While the recent improvement in accounting standards and growth in M&A activity have been welcome, they have also exacerbated the shortage of accounting professionals.

Taxation and M&A: Preferential tax treatment of initial public offerings remains a problem. Under current regulations, if a company is sold in an M&A transaction before the IPO listing, a 26% capital gains tax rate applies, whereas if the founding shareholder of a company "goes public" and then sells shares of the company into the market, a capital gains tax rate of only 13% applies (if the sale is within the first year after listing). Alternatively, after waiting one year, the entrepreneur can take advantage of an even lower tax rate of only 1% of gross transaction proceeds.

Bankruptcy Laws: Smooth and flexible bankruptcy procedures make it easier for a corporation and its assets to be acquired or merged in a "rescue" format, thereby preserving employment and protecting underlying corporate value. Legal proceedings for disposal of insolvent corporations in Japan were carried out in accordance with the Bankruptcy Law (tousanho), the Composition Law (wagi), the Corporate Reorganization Law (kaisha kosei), and the Commercial Rearrangement Law (kaisha seiki), and special liquidation (tokubetsu seisan). The Ministry of Justice conducted a review of Japanese insolvency laws, with an emphasis on reorganization-type disposition procedures covering small and medium-sized enterprises, and the Civil Reconstruction Law (minji saisei) was enacted and entered into force in April 2000. This reconstruction-type bankruptcy law replaces the Composition Law and provides improved protection of debtor assets prior to the start of rehabilitation procedures, eased requirements for beginning rehabilitation procedures, simplified and rationalized procedures for the examination and determination of liabilities, improved procedures for approval of rehabilitation plans. Legislative proposals for the fall 2002 Diet session revising the Corporate Reorganization Law to simplify disposition procedures for larger corporations undergoing reorganization are expected for implementation in spring 2003. The GOJ has also announced a plan to revise the Bankruptcy Law in FY03.

Credit Markets: Domestic and foreign investors have free access to a variety of credit instruments at market rates. In general, foreign companies in Japan have not experienced significant difficulties in obtaining funding. Most foreign firms secure short-term credit by borrowing from Japanese commercial banks or one of the many (close to one hundred) foreign banks operating in Japan. Medium-term loans are available from commercial banks, as well as from trust banks and life insurance companies. Large foreign firms have tended to use foreign sources for long-term financial needs, although increasingly sophisticated derivatives products are becoming available to assist in hedging foreign investors' perceived risk.

A.10. Political Violence: Rare to Unknown

In general, political violence is rare in Japan, and acts of political violence involving American business interests are virtually unknown.

A.11. Corruption: Evolution Towards Stricter Ethical Standards

The penal code of Japan covers crimes of official corruption. An individual convicted under these statutes is subject, depending on the nature of the crime, to penal servitude ranging from one month to fifteen years, and possible fines up to three million yen or mandatory confiscation of the monetary equivalent of the bribe.

While corruption usually involves the exchange of moneys, the methods by which business is conducted in Japan can often lead to what some foreign Japan-watchers have described as "institutionalized corruption." For example, the web of close relationships between Japanese companies, politicians, government organizations, and universities has been said to foster an inwardly-cooperative business climate that is conducive to the awarding of contracts, positions, etc. within a tight circle of local players.

Amakudari is the practice whereby senior government officials retire into top positions in Japanese companies, usually in industries that they once regulated. These officials then function as in-house consultants on regulatory matters and as lobbyists to their former ministries and agencies. *Amakudari* individuals are particularly common in the financial, construction, transportation, and pharmaceutical industries -- which, not coincidentally, are traditionally heavily-regulated industries. Foreign companies usually do not enjoy such pipelines into the bureaucracy, and thus are somewhat disadvantaged in their ability to understand and deal with laws, regulations, and informal ministry guidance. This disadvantage has been ameliorated somewhat in recent years by the introduction of more transparent administrative procedures.

While there have been some high profile exposures -- particularly over the past year -- of officials having either given or accepted bribes, the Japanese government has not had an aggressive record of criminal prosecution. Those prosecuted have generally received suspended sentences. In some cases, the government is in the dilemma of deciding how to handle past activities such as "wining and dining" which were commonplace at the time, but which are now more explicitly banned. The recent revelation of several corruption scandals may reflect an evolution towards stricter ethical standards.

Following reform in 1993, numerous shareholder civil suits have been filed. Japanese law also provides for company directors to be found personally liable for the amount of the bribe, and

some judgments have been rendered against company directors. This change may significantly impact the payment of bribes, as individuals are held personally liable without the shield of the company to protect them, although there is currently discussion within the ruling political party of new rules to make it harder to file shareholder derivative lawsuits.

Japan has also ratified the OECD Anti-Bribery Convention, which bans the bribing of government officials in countries outside Japan. The OECD has identified some deficiencies in Japan's implementing legislation, which the Government of Japan has committed to rectify.

In June 2001, Japan made amendments to the Unfair Competition Prevention Law which closed the important loophole for foreign subsidiaries and extended the definition of "foreign official" to include executives of parastatal enterprises. Other changes recommended by the OECD Bribery Working Group, such as increasing the level of penalties for bribery, extending national jurisdiction to cover the crime of bribery, and providing for confiscation of bribery proceeds, are still under consideration by the Ministry of Justice.

B. Bilateral Investment Agreements: Continuing Discussions under EPG

The 1952 U.S.-Japan Treaty of Friendship, Commerce, and Navigation gives national treatment and most favored nation treatment to most U.S. investments in Japan.

U.S.-Japan Investment Arrangement: U.S. Government concerns regarding barriers to foreign investment in Japan continue to be addressed through bilateral discussions under the U.S.-Japan Economic Partnership for Growth (EPG), established by President Bush and Prime Minister Koizumi in June 2001. The Investment Initiative Working Group has conducted a full year of meetings discussing policy measures to improve the investment atmosphere in Japan and has pursued a vigorous program of public outreach. In order to increase business awareness and receptiveness to FDI, investment promotion seminars were held in the Japanese cities of Kobe, Fukuoka, and Nagoya in March 2002, and two investment symposia are planned in New York and Chicago in July 2002.

This mirrors the continuing cooperative efforts between the governments of Japan and the U.S. to reduce barriers to foreign investment in Japan in recent years. In April 2001, the Ministry of Economy, Trade and Industry (METI) with the U.S. Department of State again with JETRO hosted an investment promotion conference in New York. METI and the Department of State submitted a report of the conference findings to the President and Prime Minister at the June 2001 Summit meeting.

On March 1, 2000, the Ministry of International Trade and Industry of Japan, U.S. Department of State and JETRO jointly hosted the "Investment-in-Japan 2000 Symposium" in Tokyo, under the auspices of the U.S.-Japan Investment Working Group. The Symposium brought together more than 30 leading experts on investment and business from the corporate, academic and government sectors of both nations. In July 2000, the Department of State and MITI transmitted to the president of the United States and Prime Minister of Japan a report based on the discussions at the Investment Symposium.

In May 1999, the Working Group issued a detailed Joint Report to President Clinton and Prime Minister Obuchi concerning improvements in the environment for foreign investment in

Japan and the U.S. Through this report, both governments emphasized the usefulness of increasing foreign investment flows into Japan and stressed their willingness to examine measures identified as important to improving the environment for foreign direct investment. In the report, the Working Group concluded that considerable steps have been taken toward improving the environment for foreign direct investment in Japan, and that improvement in Japan's environment for foreign direct investment is accelerating. At the same time, the Report noted that additional steps are both necessary and worthwhile. The Working Group met again in October 1999 and April 2000 to review progress.

Other meetings in recent years have focused on measures to improve the M&A environment in Japan, increase real estate market liquidity, and improve labor mobility. Expert hearings were held on these three subjects in July 1998. In addition, the Working Group organized two public symposia on M&A-related issues, and one public symposium on ways to improve Japanese local government investment incentives.

C. OPIC And Other Investment Insurance Programs: Not Available

OPIC insurance and finance programs are not available in Japan. Japan has been a member of the Multilateral Investment Guarantee Agency (MIGA) since it was established in 1988. Japan's capital subscription to the organization is the second largest among member countries, after the United States.

D. Labor: Toward More Flexibility

The Japanese labor market today suffers from demographic, macro-economic, and structural pressures, which are beginning to change traditional Japanese employment practices. The regulatory philosophy that has formed Japan's post-war labor laws is also changing. Foreign investors seeking to hire highly qualified workers in Japan will welcome most of these changes.

Japanese employment practices have been said to rest on "three pillars:" lifetime employment, seniority-based wages, and enterprise unions. In fact, these three aspects of the Japanese labor market have always applied only to the larger firms, and today all three are undergoing transformation. Demographic pressures – fewer young workers and a rapidly aging labor force – as well as the need for structural changes in the Japanese economy are forcing most firms to abandon both lifetime employment guarantees and seniority-based wages in favor of merit-based pay scales and limited-term contracts. Also, although labor unions play a role in the annual determination of wage scales throughout the economy, only 20.7 % of Japanese workers were union members in 2001. In firms with less than 100 employees, only 1.3 % were unionized in 2001.

Investors should be aware of Japan's high wage structure. In 2001, workers earned an average of approximately 305,800 yen per month (1.2 % increase from the previous year) in base wages including benefits, with significant variations by education, age/seniority and position. Occupational wage differentials are much smaller than in most countries. However, the Japanese Federation of Employers estimates that base wages, including basic benefits, were only 72.7 % of total wage costs in 2001. Annual summer and year-end bonuses added, on average, another 27.3 %. Relatively high statutory welfare contributions are also required for basic government pensions, health and accident insurance, and unemployment insurance. Most companies also

incur other employee welfare costs for family and/or transportation allowances, company-provided pension schemes, and such in-kind payments as housing for some employees. Offsetting these high wage costs, of course, is the fact that the Japanese work force is highly educated, disciplined, loyal to their employer, and motivated to assure the economic well-being of the company.

Japanese workers have traditionally been classified as being either "regular" or "other" employees and this system is, to a considerable degree, still in place today. Regular employees are usually recruited directly from schools or universities and given an employment contract with no fixed duration. Other employees are given fixed duration employment contracts, which generally cannot exceed one year but may be renewed several times over. Still other employees include part-timers, interns, and "dispatched workers" —as workers from temporary work agencies are called in Japan. Until very recently, only a few occupations could be handled by dispatched worker agencies but this is one area where Japanese labor law has in fact been deregulated, thus the number and types of dispatched workers have increased geometrically over the past several years.

The regulation of private, fee-charging employment agencies — including executive search firms — has also recently been liberalized. Although a fairly time-consuming and bureaucratic licensing procedure is still required, private employment agencies can now serve virtually the entire range of occupations. On-line, Internet based, job seeking and placement services are, however, still in their infancy in Japan — constrained at least partly by a Ministry of Labor requirement that every employment agency must personally interview each of its clients.

Defined contribution pensions, introduced in October 2001, should promote labor mobility, as workers will be able to carry their pension funds to other jobs.

E. Foreign-Trade Zones/Free Ports: None

Japan no longer has any free-trade zones or free ports. Customs authorities, however, do allow the bonding of some warehousing and processing facilities in certain areas adjacent to ports on a case-by-case basis. The GOJ established a law in 1992 entitled the "Law on Extraordinary Measures for the Facilitation of Imports and Foreign Direct Investment in Japan" (effective July 1992 and valid until May 2006). Under the law, the GOJ helps increase access to the Japanese market for foreign goods and capital at government-designated "foreign access zones" near harbors and airports.

F. Capital Outflow Policy: Net Exporter of Capital

Japan has generally continued to be a net exporter capital.

G. Investment Data: FY 2001 Reflects Downturn

The following tables incorporate JFY01 data for both inward and outward foreign investment in Japan. The data show a considerable drop following the sharp increase in U.S. investment in Japan in FY 99 and 00. Total foreign investment in Japan, dominated by the Netherlands and the U.S., decreased about 40 % in JFY 01, although still up over 300% since

JFY97. Japanese investment overseas dropped in JFY01, but the overall ratio of inward to outward FDI remained nearer OECD average levels.

The number of cases of U.S. FDI in Japan was up 19% over the previous year, but the value decreased by 60%. New investment was concentrated in telecom and financial services, while on the manufacturing side investment in machinery and chemicals were still most significant.

The official statistics below represent notification to the Ministry of Finance (MOF) of authorization by MOF of specific planned investment projects (as reported to MOF by companies), not necessarily actual flows of investment. Thus these figures generally exceed by a substantial amount actual investment flows as reported in Japan's balance of payments data. (At the same time, neither the data below nor the balance of payments statistics capture re-investment of profits by foreign firms operating in Japan, or Japanese firms operating overseas. Therefore, according to some academic researchers, both types of official data mis-state actual foreign capital investment by a wide margin.)

All data in the tables below is from MOF, current as of June, 2002, and converted into dollars using each year's average exchange rate: JFY98 at 128.02 yen to the dollar, JFY99 data at 111.54 yen to the dollar and JFY00 data at 109.00 yen to the dollar, JFY01 data at 125.60 yen to the dollar.

Table 1: Annual New FDI into Japan (Billions of Dollars)

JFY	1992	1993	1994	1995	1996	1997	1998
	4.08	3.08	4.16	3.83	6.84	5.53	10.47
JFY	1999	2000	2001				
	21.5	28.0	17.3				

Ratio of Japan's Inward to Outward FDI Flows

JFY
1992 - 1:8.4
1993 - 1:11.7
1994 - 1:9.9
1995 - 1:13.4
1996 - 1:7.02
1997 - 1:9.77
1998 - 1:3.9
1999 - 1:3.1
2000 - 1:1.7
2001 - 1:1.8

Table 2: Foreign Direct Investment in Japan, by country
(Million dollars; annual flow; reporting basis)

	JFY 1999	JFY 2000	JFY 2001	Cumul.tot. '89-'01
N. America	3,742	9,887	5,511	42,369
U.S.	2,230	9,268	5,119	32,851
Canada	1,512	618	390	4,396
Europe	12,674	6,320	8,725	45,371
Neth'lds	4,224	475	6,550	17,823
U.K.	805	513	1,160	4,927
Germany	419	2,566	97	5,990
Switz.	344	1,993	213	4,754
France	6,685	276	107	8,202
Asia	986	383	451	5,540
Singapore	661	88	247	2,713
Taiwan	118	222	150	937
Hong Kong	108	17	26	1,148
Korea	95	49	24	561
L. Americ	2,595	1,541	516	7,921
Cayman Isles	2,257	1,209	369	4,713
BVI	209	63	107	1,634
Bermuda	56	235	20	957
*Japan	1,448	10,471	2,100	20,206
Total	21,511	28,671	17,340	121,791

ASTERISK: Investments from Japan are those by foreign-owned firms in Japan.

Table 3: Foreign Direct Investment in Japan, by industry
(Million dollars; annual flow; reporting basis)

				Cumul.total
	JFY 1999	JFY 2000	JFY 2001	'89-'01
Manufact.	8,783	7,254	2,611	39,693
Machinery	7,757	3,228	1,103	22,458
Chemicals	541	1,640	920	9,318
Metals	160	17	1	1,431
Rubr/Lthr	63	10	56	746
Petroleum	121	2,352	70	3,251
Textiles	2	22	22	175
Foods	13	0	280	945
Glass/Cer	51	0	75	177
Other	76	11	84	1,192
Non-manuf.	12,727	21,417	14,729	82,097
Finance/Ins1	4,586	9,443	5,261	28,546
Trade	3,124	2,536	865	17,297
Services	1,845	2,170	1,325	14,473
Real Estate	151	317	586	3,496
Telecom	2,959	6,888	6,597	17,061
Transport	20	52	18	355
Construction	20	0	68	159
Other	22	11	6	710
Total	21,511	28,671	17,340	121,791

Table 4: U.S. Direct Investment in Japan, by industry
(Note: Data is actually, North America, not U.S.)
(annual flow; reporting basis)

	JFY 2000		JFY 2001	
	\$ Million	# of cases	\$ Million	# of cases
Manufact.	1,909	37	775	44
Machinery	828	24	581	28
Chemicals	553	7	179	8
Metals	27	1	--	--
Foods	--	--	--	--
Non-manuf.	7,977	637	4,736	411
Finance/Ins.	6,360	98	3,447	101
Commerce/Trade	228	148	529	75
Services	980	343	409	191
Real Estate	28	24	50	23
Telecom	403	20	230	16
Construction	--	--	68	4
Total	9,887	674	5,511	455

Table 5: Japanese Direct Investment Overseas, by country

(Million dollars; annual flow; reporting basis)

	JFY 1999	JFY 2000	JFY2001	Cum.tot. '89-'01
N. America	24,770	12,442	6,434	278,058
U.S.	22,295	12,306	6,346	266,269
Canada	2,474	137	884	117,875
Europe	25,804	24,747	10,532	177,933
U.K.	11,718	19,408	3,945	86,474
Netherlands	10,360	2,795	4,490	43,264
Germany	649	324	416	10,753
France	1,127	330	307	11,924
Ireland	460	49	123	3,733
Spain	518	33	42	3,718
Sweden	n/a	847	2	1,018
Asia	7,162	6,014	6,154	114,756
Thailand	816	944	877	15,139
Indonesia	918	419	459	18,071
China	751	1,008	1,435	20,507
Singapore	962	429	974	14,135
Hong Kong	971	949	295	15,419
Malaysia	525	235	255	8,901
Philippines	617	464	753	5,983
South Korea	980	824	541	6,411
India	208	170	144	2,014
Taiwan	285	517	318	5,479
Vietnam	99	22	77	1,338
L. America	7,437	5,306	7,630	70,580
Cayman Isles	2,242	2,774	4,978	24,741
Panama	1,413	1,318	967	19,199
Brazil	654	228	1,365	8,983
Mexico	1,484	211	44	3,769
Bermuda	145	553	224	4,930
Oceania	894	676	525	32,150
Australia	857	521	492	27,598
Africa	515	54	192	6,131
Liberia	217	42	118	4,940
South Africa	157	12	66	747
Middle East	113	19	20	2,796
UAE	n/a	-	8	640
Israel	2	8	12	65
Total	66,694	49,257	31,487	682,407

Table 6: Japanese Direct Investment Overseas, by industry
(Million dollars; annual flow; reporting basis)

	JFY 1999	JFY 2000	JFY 2001	cum.tot. '89-00
Manufacturing	42,310	11,845	13,893	236,111
Electrical	16,350	3,090	3,646	70,111
Chemicals	1,694	1,942	1,486	29,641
Transport	4,781	3,182	4,138	13,263
Food	14,908	261	815	26,239
Metals	1,458	717	633	17,017
Machinery	995	1,430	1,214	19,039
Lumber/Pulp	116	150	729	5,646
Textiles	260	226	202	7,877
Other	1,749	849	846	25,288
Non-manufact.	24,178	37,158	17,312	438,925
Finance/Ins.	9,885	8,523	10,712	129,187
Comm/Trade	3,877	3,391	2,568	64,120
Real Estate	2,114	370	523	85,267
Services	4,314	1,784	1,545	84,639
Transport	2,771	22,185	1,335	51,532
Mining	922	650	478	16,230
Construction	182	91	64	4,870
Ag/Forestry	81	27	33	1,643
Fisheries	26	134	27	1,075
Other	8	2	26	367
Total	66,694	49,257	31,487	243,164

Table 7: Foreign Direct Investment in Japan relative to GDP

	JFY1996	1997	1998	1999	2000	2001
Nominal GDP (a) (trillion yen)	504.4	507.6	487.3	493.8	511.8	500.3
FDI Inflow (b) (trillion yen)	0.77	0.68	1.34	2.4	3.1	2.2
b/a (%)	0.15	0.13	0.27	0.49	0.61	0.44
Source: Japanese Ministry of Finance, June 2001						

Table 8. Examples of Major Foreign Direct Investments by US companies and other Foreign Nations' companies

Financial/Insurance Services

Merrill Lynch - acquired Yamaichi securities
GE Capital - acquired Toho Insurance
Manulife (Canadian) - acquired Daihyaku Insurance
Ripplewood - acquired Long Term Credit Bank
AIG - acquired Chiyoda Life Insurance
Prudential - acquired Kyoei Life Insurance

Information Technology/Telecommunications

C and W (British/US interest) acquired IDC
MCI World Com - Greenfield investment
Level 3 - Greenfield investment
Time Warner/Media One - TITUS
Global One (Sprint JV with European firms) -greenfield investment
Cisco Systems -capital participation in Soft Bank

Distribution/Retail/Hotel

Toys-R-US
Costco
Sports Authority
GAP
Disney stores
Nike
Amazon.com
Starbucks
Ripplewood - acquired Phoenix SEAGAIA Resort
Walmart (Business tie-up with Seiyu Supermarket)

Manufacturing

(tie ups)

Renault-Nissan
Ford-Mazda
GM-Suzuki
Daimler-Chrysler
GE - acquired Kawasaki LNP (Kawasaki Steel's chemical manufacturing subsidiary)
Dow Chemical - acquired Leich Hold (Dai Nippon Chemical's subusidiary)
IBM- acquired Display Technology (Toshiba's CD/LSD manufacturing subsidiary)
Solectron - acquired NEC's PC manufacturing business department)

Micron Technology -acquired KMT Semiconductor (Kobe Steel's semiconductor manufacturing subsidiary)